

ANNUAL REPORT

of

ALLIED STORES CORPORATION

FOR THE FISCAL YEAR ENDED JANUARY 31, 1942

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ALLIED STORES CORPORATION

1440 BROADWAY
NEW YORK, NEW YORK

DIRECTORS

C. C. ANDERSON C. C. Anderson Stores Company, Boise, Idaho	R. C. KRAMER New York, N. Y.
EDWARD W. BROIDY Allied Stores Corporation	PAUL M. MAZUR Lehman Brothers, New York, N. Y.
JOSEPH CHAPMAN Minneapolis, Minn.	CHARLES E. MCCARTHY Allied Stores Corporation
ALBERT COONS Allied Stores Corporation	EDWARD R. MITTON Jordan Marsh Company, Boston, Mass
PERCY J. EBBOTT The Chase National Bank, New York, N. Y.	G. W. MITTON Jordan Marsh Company, Boston, Mass.
J. LESTER EISNER Sigmund Eisner Company, New York, N. Y.	B. EARL PUCKETT Allied Stores Corporation
ROBERT R. GUTHRIE New York, N. Y.	EUSTACE SELIGMAN Sullivan & Cromwell, New York, N. Y.

HAROLD J. SZOLD
Lehman Brothers, New York, N. Y.

OFFICERS

B. EARL PUCKETT	President
EDWARD R. MITTON	Vice-President
ALBERT COONS	Vice-President
EDWARD W. BROIDY	Vice-President
CHARLES E. MCCARTHY	Vice-President
ROBERT W. PYKE	Vice-President
ARTHUR C. HALLAN	Secretary-Treasurer

TRANSFER AGENT

Preferred and Common Stocks
THE COMMERCIAL NATIONAL BANK AND TRUST COMPANY OF NEW YORK
46 Wall Street, New York, N. Y.

REGISTRARS

Preferred Stock

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK,
11 Broad Street, New York, N. Y.

Common Stock

THE NEW YORK TRUST COMPANY
100 Broadway, New York, N. Y.

TRUSTEE FOR FIFTEEN-YEAR $4\frac{1}{2}\%$ DEBENTURE BONDS, DUE APRIL 1, 1950,
AND $4\frac{1}{2}\%$ DEBENTURES DUE 1951
BANKERS TRUST COMPANY 16 Wall Street, New York, N. Y.

ALLIED STORES CORPORATION
1440 BROADWAY
NEW YORK, NEW YORK

May 7, 1942

To the Stockholders:

In the following paragraphs, the operating results of Allied Stores Corporation and subsidiary companies for the fiscal year ended January 31, 1942, (hereinafter referred to as the year 1941) and the financial condition at the close of the period are briefly summarized. Consolidated statements of profit and loss, earned surplus and capital surplus for the year, and a consolidated balance sheet, with supporting schedule of funded debt, at the close of the year, certified by Ernst & Ernst, the Company's public accountants, are included as part of this report.

Retail Sales

In Terms of Value:

Dollar sales volume, \$151,808,858, was again the highest in the history of the Company and was 25.2% greater than in the preceding year. B. Gertz, Inc., a subsidiary acquired at the beginning of the year and operating a department store in Jamaica, Long Island, New York, contributed 5.6% of this percentage increase. Dollar sales volume compared with the years immediately preceding follows:

	Value	% Increase
1941	\$151,808,858	25.2
1940	121,270,682	8.2
1939	112,122,354	8.6
1938	103,243,425	— 4.0
1937	107,556,225	—

In Terms of Sales Transactions:

The number of items of merchandise sold based on the number of sales transactions was also the highest in the history of the Company and 8.6% greater than in the preceding year. Of this 8.6% in-

five

crease 3.5% was contributed by B. Gertz, Inc. The percentage increase in the number of sales transactions was not as large as the percentage increase in dollar sales due (a) to an increase in retail price levels which averaged for the year approximately 9%, (b) to consumers desiring and being able to purchase merchandise of a slightly higher quality, and (c) to a somewhat greater than proportionate increase in business in relatively high unit price merchandise. The following shows a comparison of the number of sales transactions for each of the past five years:

	Sales Transactions	% Increase
1941	78,400,000	8.6
1940	72,200,000	3.9
1939	69,500,000	5.9
1938	65,600,000	1.4
1937	64,700,000	—

Profits

Profit and Federal Taxes:

Profit before federal taxes on income would have been \$10,961,078 if the Company had not changed its method of valuing inventories. Such profit, however, was reduced \$1,276,339 by the adoption of the "last-in, first-out" method of determining cost of certain inventories and \$190,481 by the elimination of cash discounts from beginning and closing inventories. These changes in methods of valuing inventories resulted in reductions in provision for federal taxes on income, \$775,000,* and in final consolidated net profit, \$691,820. The following shows comparisons for each of the past five years of profit before federal taxes on income, provision for federal taxes and consolidated net profit:

Year	Profit Before Federal Taxes on Income	Provision for Federal Taxes	Consolidated Net Profit
1941	\$9,494,258	\$4,200,000	\$5,294,258
1940	5,353,129	1,355,000	3,998,129
1939	4,155,585	720,000	3,435,585
1938	2,758,720	525,000	2,233,720
1937	3,673,206	769,000	2,904,206

* NOTE: In this connection, reference is made to the final paragraph of Note B to financial statements.

Profit per Share:

In the following tabulation consolidated net profit is expressed in terms of profit per share of 5% Preferred Stock and, after deducting dividends paid on such preferred stock, of profit per share of common stock, for each of the last five years:

	Profit per Share of Preferred Stock	Profit per Share of Common Stock
1941	\$22.30	\$2.27
1940	17.57	1.57
1939	15.01	1.26
1938	9.63	.59
1937	12.50	.96

Profit Trends by Quarters:

A five year comparison of profits, by quarters, follows:

Profit Before Federal Taxes on Income:

	1937	1938	1939	1940	1941
First quarter ... \$	770,203	\$ 365,447	\$ 392,478	\$ 462,211	\$1,597,595
Second quarter	160,017	610,334*	103,814*	235,856	1,101,173
Third quarter...	1,166,059	992,552	1,319,051	1,513,756	2,825,255
Fourth quarter	1,576,927	2,011,055	2,547,870	3,141,306	3,970,235
Total Year	3,673,206	2,758,720	4,155,585	5,353,129	9,494,258
Federal taxes on income	769,000	525,000	720,000	1,355,000	4,200,000
Consolidated net profit	\$2,904,206	\$2,233,720	\$3,435,585	\$3,998,129	\$5,294,258

* Loss

Working Capital

Cash, \$3,636,068, was over one million dollars greater than at the beginning of the year. Notes payable to banks, \$2,900,000, was two million greater. The ratio of current assets, \$50,881,163, to current liabilities, \$20,315,750, was 2.5 to 1 at the close of the year which compares with 3.6 to 1 at the beginning of the year. This reduction in ratio resulted from an increase in merchandise inventories, with consequent increases in bank loans and trade ac-

counts payable, and the substantial increase in federal tax liability. Net current assets — current assets minus current liabilities — increased \$1,869,886 during the year. Net current assets at the close of the year for each of the last five years follow:

	Net Current Assets
1941	\$30,565,413
1940	28,695,527
1939	27,317,699
1938	27,845,922
1937	28,279,130

Accounts Receivable:

Customers' accounts receivable (net) at the close of the year were \$22,449,461 or \$4,212,796 more than at the beginning of the year. This increase was composed of increases in current accounts, \$2,962,583, in deferred accounts, \$1,352,852 and in the reserve provision for losses in collection, \$102,639. B. Gertz, Inc., acquired during the year, contributed \$666,372 of the increase in current accounts and \$386,473 of the increase in deferred payment accounts. Eliminating these accounts of B. Gertz, Inc., the increase in current accounts was \$2,296,211 or 20%, and the increase in deferred payment accounts was \$966,379 or 13%.

The current trend of deferred payment accounts is downward. Government regulation of such accounts as to amount of down payment required and length of time permitted are contributing factors. The unavailability of certain lines of merchandise usually sold on this basis, such as refrigerators, washing machines, radios, sewing machines, bicycles, typewriters, etc., will be a strong influencing factor in the future in this respect.

The amount of the reserve for doubtful accounts at the close of the year was established, as in preceding years, by an age analysis of each individual account. All balances over six months past due on current accounts and all installments over one month past due on deferred payment accounts are 100% reserved. Based on age analyses of the individual accounts and on past experience, all other balances are believed to be adequately reserved.

Inventories:

Merchandise inventories at the close of the year, \$24,215,448, were \$5,815,469 greater than at the beginning of the year. Of this increase B. Gertz Inc., acquired during the year, contributed \$945,019, leaving an increase on a comparable store basis of \$4,870,450. At the close of the year 85.4% of all inventories in the stores was less than six months old and 95.4% less than one year old. These percentages compare with 78.5% and 91.7%, respectively, at the beginning of the year and with 80.0% and 92.7% at January 31, 1940. General price levels of merchandise were higher at the close of the year than at the beginning. A given quantity of identical merchandise would be valued higher at the close of the year than at the beginning under these conditions and following inventory practices previously used. A book profit would result without a corresponding increase in actual assets. This book profit, in effect, would simply represent a writeup of values. In periods of normal price trends and only minor fluctuations in price levels this is not a serious factor. When price levels rise or fall substantially, however, the effects become quite important.

A method of establishing inventory costs, known as "last-in, first out," reflects more accurately results of operations in periods of widely varying price levels. Its use tends to stabilize carrying values of inventories, and therefore profits. More realistic policies during periods of rapidly rising or falling prices affecting dividends, wages, employment and expansion should result. Many large industrial companies have used this method for a number of years. The accounting profession has recognized its adaptability to retail stores by the use of price indices and has approved its use. The Company has adopted the "last-in, first-out" method of valuing those parts of its inventory to which the method is most applicable. As a result, the valuation of those inventories was reduced \$1,276,339.

Merchandise is usually purchased by retailers on terms of a stated invoice cost with a provision for a percentage discount from the face of the invoice if payment is made within a stated period. Accounting practices differ in the retail field as to method of handling such discounts. Some companies treat the invoice price as the cost of the merchandise and the cash discount as financial profit or income at

the time the bill is paid. Other companies consider the cash discount as a reduction from the invoice price of the merchandise.

On an annual basis profits are the same under either method except for variations in the amounts of inventories and accounts payable as between the beginning and closing of the year. From a balance sheet viewpoint there is also a difference. The principle of considering cash discounts as a reduction in the cost of the merchandise gives a lower and therefore a more conservative valuation of the inventory.

At the inception of the Company a majority of the subsidiaries acquired were treating cash discounts as financial income at the time of payment of invoices and were therefore considering the invoice price as the true cost of merchandise. The Company adopted this common practice of the subsidiaries acquired in the preparation of its reports and has followed that practice consistently. Partially in recognition of the fact that this practice did not give the most conservative inventory valuation permissible, the Company has carried a reserve on its balance sheet entitled "Reserve for Contingencies, Revaluation of Merchandise, Etc."

The Company decided during the year to adopt the accounting practice of eliminating cash discounts from the cost valuation of its inventories. As a result, inventories are shown on the accompanying balance sheet \$1,075,616 less than if the Company had not made this change.

Fixed Assets

The Company's investment in land, buildings, equipment, and fixtures at the close of the year, \$33,861,777, was \$602,017 more than at the beginning of the year. This increase was made up of fixtures and equipment of B. Gertz, Inc., at the date of acquisition, \$125,677, and net additions and improvements for all stores during the year, \$1,843,188, offset by depreciation charged to expense during the year \$1,366,848.

As in previous years certain stores were air-conditioned and others were expanded or modernized. Stores for which more than normal expenditures were made include: The A. Polsky Company, Akron, Ohio; The Bon Marche, Seattle, Washington; The Titche-Goet-

tinger Company, Dallas, Texas, and the James Black Dry Goods Company, Waterloo, Iowa. Additions and improvements to physical plants for the immediate future will of necessity be confined to necessary repairs and replacements and minor department rearrangements. All modernization and expansion programs of major importance that would conflict with the war effort in their demand for skilled labor or materials are being deferred.

Maintenance and Repairs:

The Company continued its policy throughout the year of maintaining its buildings, equipment, and fixtures in good physical condition. The amount charged to operating expense for maintenance and repairs was \$1,107,500. Combining the provision for depreciation with the direct expense charges for maintenance and repairs, operations for the year were charged with approximately two and one-half million dollars for depreciation and maintenance of buildings, equipment, and fixtures. Combining the amount expended for maintenance and repairs with cost of additions and improvements, cash disbursements for fixed assets for the year were approximately three million dollars.

Long-Term or Funded Debt

Parent Company:

There were outstanding at the beginning of the year \$82,375 Fifteen Year $4\frac{1}{2}\%$ Debenture Bonds, due April 1, 1950, \$4,348,000 $4\frac{1}{2}\%$ Debentures due 1951 and a \$1,500,000 six-year bank loan. The Company reacquired during the year \$7,000 principal amount of Fifteen-Year $4\frac{1}{2}\%$ Debenture Bonds, due April 1, 1950. The amount of $4\frac{1}{2}\%$ Debentures due 1951 at the close of the year was the same as at the beginning. Sinking fund requirements for the year on these bond issues were met from bonds held in the treasury at the beginning of the year. The first annual installment on the \$1,500,000 six-year bank loan was paid during the year, reducing this loan to \$1,250,000. The parent company at the beginning of the year was partially obligated as guarantor for a subsidiary on a real estate mortgage. This subsidiary was absorbed during the year, resulting in the parent company assuming full obligation on this mortgage of \$690,000.

All outstanding Fifteen-Year $4\frac{1}{2}\%$ Debenture Bonds, due April 1, 1950, \$75,375, have been called against cash payments at par for retirement July 1, 1942. All outstanding $4\frac{1}{2}\%$ Debentures due 1951 held in the treasury, \$32,000, plus \$143,420 in cash, representing the call price on \$142,000 face value of bonds, will be required to meet current year's sinking fund obligations. A second instalment of \$250,000 on the six-year bank loan will be payable during the year. Amortization, payable during the year, on the real estate mortgage mentioned above, amounts to \$40,000. These cash payments, together with the current year's amortization requirements on subsidiary funded debt, are shown as a current liability on the accompanying balance sheet.

Subsidiary Companies:

Bonds, mortgages, and notes of subsidiary companies outstanding at the beginning of the year totaled \$14,406, 651. A subsidiary obtained a \$250,000 five-year bank loan during the year to help finance an addition to its building. Amortization payments for the year totaled \$558,789. The Company acquired during the year \$290,000 face amount of the income bonds of a subsidiary. The holders of \$21,393 of income bonds of a subsidiary exercised their option to convert such bonds into the Company's 5% Preferred Stock during the year. These transactions, together with the Company's assuming full liability on the \$690,000 mortgage mentioned above, left the long-term or funded debt of subsidiaries at the close of the year at \$13,096,469.

The Indenture of the Jordan Marsh Company First Mortgage and First Lien $4\frac{3}{8}\%$ Fifteen-Year Sinking Fund Bonds due 1951 was modified during the year whereby maturity was extended to August 15, 1956, the interest rate was reduced to $3\frac{3}{4}\%$ and the semi-annual payments for amortization and interest were reduced from \$227,000 to \$168,750.

Reserve for Contingencies:

The reserve for contingencies, revaluation of merchandise, etc., at the beginning of the year amounted to \$1,671,786.89. Adoption of the "last-in, first-out" method of inventory valuation resulted in a reduction of inventory values of \$1,276,339. Eliminating the cash

discount content of inventory values also reduced the value of ending inventories \$1,075,616. Due to these changes in methods of valuing inventories it was decided to transfer \$1,171,786.89 from this general reserve to capital surplus. The remaining balance of \$500,000 was retained as a reserve for general contingencies.

Acquisition and Liquidation of Subsidiaries:

As previously reported, the Company acquired the entire capital stock of B. Gertz, Inc., in February 1941. The cost of this acquisition was \$1,616,900, payable \$400,000 in cash and the balance by the issuance of 12,169 shares of the Company's 5% Preferred Stock. This acquisition has proved to be a profitable one. Since the inception of the Company, a subsidiary, Rudge & Guenzel Company, has operated a department store in Lincoln, Nebraska. This has never been a profitable unit. In December, 1941 this subsidiary sold its accounts receivable, merchandise inventories and fixed assets, effected a cancellation of its lease obligations, and ceased operations.

General

A more comprehensive treatment than it is practical to give in this letter is accorded certain subjects believed to be of interest to stockholders under captions:

1. General Aspects of the Company and Its Objectives.
2. The Company's 5% Preferred Stock.
3. The Company's Common Stock.
4. Problems of the Retailer in This War Economy.

Conclusion

While the year 1941 was one of general strife and turmoil throughout the world and was filled with happenings and changes of great social, political, and long-term economic significance, the eventual effects of which cannot be visualized at this time, it was a year of constantly increasing industrial and business activity, and therefore a favorable year for retailing. Your Company took advantage of these opportunities, as is shown by its record of sales and profits.

Conditions of late 1941 continue into 1942, intensified in character and accelerated in pace. The future is of course quite unpredictable. No one can do more than guess even as to the immediate future, its problems and opportunities. Your management is confident, however, that, due to the intense program of education and executive development that has been followed for the past several years, your Company is in a position to meet problems and difficulties or to take advantage of opportunities, as the case may be, with relatively satisfactory results.

Respectfully submitted,

Two handwritten signatures in black ink. The signature on the left is stylized and appears to be 'J. H. H.'. The signature on the right is more cursive and appears to be 'E. H. H.'.

GENERAL ASPECTS OF THE COMPANY AND ITS OBJECTIVES

The history of the Company, its scope, principles of operation and organization, and its purpose and future possibilities have been discussed in previous reports to stockholders. The following brief summarization of these discussions is included herein so that this report may be reasonably comprehensive and self-contained.

Brief History

Allied Stores Corporation was organized as Hahn Department Stores, Inc. (name changed in 1935) only a few months before the beginning of the severe depression which started in the autumn of 1929. The central office executive organization was as yet unproven and methods of administration and operation were only in the process of development when the depression began. It was most unfortunate that a new organization had to cope with the problems of a major depression.

Simultaneously with the acquisition of original store subsidiaries new long-term leases were made covering many of the premises occupied by these subsidiaries. The leases were written at the all-time peak prices prevailing in the late twenties. The rental provided for under many of these new leases not only anticipated the continuance of then existing sales volume but a continuance of the trend of growth.

As a result of the organization and real estate problems, mentioned above, the effects of the depression on the Company were magnified. Much progress has been made in obtaining permanent relief from many burdensome leaseholds, in strengthening the executive organization in the stores and the central office, and in the development of a proper technique of administration and operation. The Company has been on a profitable basis since 1934. Its progress from the depth of the depression compares very favorable with that of other department store companies.

Purpose of Company

Allied Stores Corporation is primarily a holding company with its capital invested, on a permanent investment basis, in the direct ownership of two department stores, complete ownership of capital stocks of corporations owning department stores and of realty companies owning land and buildings occupied by certain of the stores. Two stores, The Bon Marche, Seattle, Washington, and Dey Brothers & Co., Syracuse, New York, are owned and operated as branches of Allied Stores Corporation while other stores are operated by wholly owned subsidiaries. Allied Stores Corporation, largely through a wholly owned subsidiary, Allied Purchasing Corporation, also maintains a comprehensive organization to perform service, advisory, and administrative supervisory functions in relation to the stores.

A highly specialized staff is maintained in the central organization, covering such fields as taxes, insurance, accounting systems and methods, consumer credits, statistical analysis and forecasting, supply purchasing, plant maintenance and improvement, store planning, display, and sales promotion. A well staffed buying office is maintained by Allied Purchasing Corporation in New York City and Chicago, covering these merchandise markets daily for the stores. The California markets and principal foreign markets are covered through the services, on a fee basis, of outside buying offices located in these markets.

Scope of Company

The Company owns and operates directly or through subsidiary companies sixty department stores and smaller stores that might be described as junior department stores, located from coast to coast in twenty-one states. In most cities in which the Company operates department stores, its unit ranks as either the first or second retail institution of the respective city from the standpoint either of character of institution, annual sales volume, or both. The twenty-two units owned through C. C. Anderson Stores Company and the six units owned through A. E. Troutman Company, both wholly owned subsidiaries, might be classified as junior department stores.

Each store unit of Allied Stores Corporation (with the minor exception of a few of the C. C. Anderson Stores Company smaller units) was an existing and well established retail institution at the time of acquisition and had been serving its community for several decades and, in certain instances, for approximately a century. Ninety percent of Allied's sales volume is obtained in units which were well-established in their respective communities in the Nineteenth Century.

Principal lines of merchandise carried in these stores are women's, men's, and children's clothing and accessories and home needs. Most of the larger stores operate basement divisions appealing to the lower income groups of consumers. In general, stores endeavor to satisfy most of the general merchandise needs of consumers from the lower income working classes up to and including those of the families of the professional man, the smaller businessman and executive.

The Company regularly employs sixteen thousand two hundred people. An additional sixty-three hundred people are employed in handling business in peak periods, such as the Christmas Season. Nine hundred sixty-eight thousand four hundred charge customers purchase approximately sixty million dollars annually from the Company's stores on a regular charge account basis, while two hundred and fifty-four thousand customers have deferred payment accounts. It is estimated that on the average one home in every twelve in the United States represents a customer of Allied Stores Corporation or its subsidiaries.

Frequently Allied Stores Corporation is presented with opportunities to acquire additional retail units. The board of directors of the Company has considered the most favorable of these proposals. Of the approximately \$152,000,000 sales volume of the Company for the year ended January 31, 1942, approximately \$33,000,000 can be attributed to stores acquired since 1934. The purchase price of stores acquired was paid partly in cash and partly in the common and preferred stocks of Allied Stores Corporation. The profit record of these stores acquired compares favorably with that of stores owned since the inception of the Company.

Principles of Operation

In general, the merchandise and promotional appeal of stores controlled by Allied Stores Corporation is the same as before they were acquired. Effort is directed to intensifying and increasing the effectiveness of each individual store in accordance with its established character rather than to change this appeal and character in order to standardize as between stores. The importance of treating each store as a separate and distinct unit with characteristics and problems peculiar to itself is stressed in the management and operations of the Company.

Allied Stores Corporation endeavors to maintain and improve customer acceptance and profit possibilities of the individual stores by making sure of the existence and effectiveness of capable and adequate management and by bringing to each unit the advantages of financial strength and the best of the most modern merchandising, promotional, and operating methods.

The executive personnel of an individual store owned by Allied Stores Corporation is very similar as to number, caliber, and function to that of independently owned and operated department stores of like size and character. The form of organization is usually changed but little, if any, when an independently owned and operated store is acquired by Allied Stores Corporation. Activities of the central organization are directed toward making the efforts of the individual store executives more effective rather than to minimizing the need for them.

The officers of Allied Stores Corporation work with the executives of the stores in the formulation of what appear to be the soundest policies, plans, and programs in regard to customer appeal, merchandise assortment, plant and equipment, personnel, etc. In formulating such policies, plans, and programs, the characteristics of that store as reflected by its history and the needs of its community receive primary consideration. The execution of such policies, plans, and programs is the responsibility of the chief operating executives of that particular store, subject to such check by officers of Allied Stores Corporation as is necessary to assure their continuance and effectiveness.

Organization of Board of Directors

The board of directors of Allied Stores Corporation holds regular monthly meetings. In addition to electing officers of the corporation the board of directors appoints an executive committee of ten of its members which, according to the by-laws of the Company, has practically all of the authority of the board of directors when the board is not in session. This executive committee includes the six chief executives of the Company who are members of the board of directors and four of the non-operating members of the board. This committee holds regular monthly meetings.

The board of directors also has appointed the four non-operating members of the executive committee as an advisory committee:

1. To study currently the operating and financial reports of the Company and to review periodically the policies, procedures, organization form and executive personnel of the Company, and to advise with the officers of the Company in regard thereto; and
2. To study proposed actions in connection with corporate, financial, real estate and acquisition problems and to make recommendations to the board of directors in regard thereto.

In addition to attending a monthly meeting of the executive committee and board of directors as members of those groups, the members of the advisory committee also hold one advisory committee meeting monthly. Special meetings of the advisory committee are called by the president of the Company when any special problem arises upon which he desires advice or counsel.

Opportunities

The Company's activities form a part of one of the most fundamental of all industries, that of distributing needed and wanted merchandise to the consumer. Laboratory discoveries or inventions of others, technological improvements, mass changes in customs or habits, and the dictates of fashion contain no hazards but rather offer opportunities to the alert retailer.

While distribution to consumers is a fundamental industry, it is also a most highly competitive one. Identical or similar merchandise is generally available to competitors at approximately the same cost price. Usually, cost prices are established by the manufacturer and retail prices by competitors. Many elements of operating expense are of a fixed or inflexible nature and are constantly becoming more so. There are no effective patents, trademarks, or copyrights that assure profits or cushion losses for the retailer. Buying and selling are each done in open competitive markets which means on a basis at which the inefficient fail. Possibilities for consistent growth and profits lie in the degree of excellency of the operation.

Competition for consumer patronage and favor not only exists between retailers of a given type but even more intensely between types of retailing. In this highly competitive field lies the Company's greatest opportunity for growth and profit. Each of these various types of retailing has its advantages and disadvantages. Company executives do not recognize the Company as necessarily representing any particular type of retailing but endeavor to secure for the Company the respective advantages of the various types. While the stores were traditionally individual, locally owned department stores and still retain the advantages of such, through central ownership and a strong central office many of the advantages of the various types of chains and other forms of mass distribution are available or attainable.

The various types of retailing are being studied constantly in efforts to discover and adapt effective ideas, policies and methods. This job requires extensive research and education. It is to such work that management looks for the future of the Company. A large group of sincere, intelligent, open-minded staff and administrative executives are directing their best efforts on the Company's behalf toward these objectives.

THE COMPANY'S 5% PREFERRED STOCK

Purchases and Retirement:

There were 227,501 shares of the Company's 5% Preferred Stock outstanding at the beginning of the year. In connection with the acquisition of B. Gertz, Inc., 12,169 shares of this stock were issued. A holder of income bonds of a subsidiary company with conversion privileges elected to convert during the year certain of these bonds into this stock. Two hundred thirteen shares of this stock were issued in exchange. The Company purchased during the year 2,500 shares of this stock at a cost of \$195,783.03. There were 237,383 shares of this stock outstanding at the close of the year.

The Company held in the treasury at the beginning of the year 2,647 shares of this stock. These shares and 697 of the 2,500 shares purchased were cancelled during the year in satisfaction of all sinking fund obligations to July 1, 1941, leaving 1,803 shares in the treasury as of the close of the year. Subsequent to the close of the year 3,000 shares were purchased at a cost of \$221,036. Practically all of these shares and the shares in the treasury at the close of the year will be cancelled to satisfy the annual sinking fund obligation due July 1, 1942.

Ownership of Preferred Stock:

There were 6,130 holders of record of the 237,383 shares of this stock on April 15, 1942, or an average of 39 shares per holder. According to the stock records of the Company and eliminating the stock in the names of brokers and known nominees held for an unknown number of people, the following summary shows the number of the holders of the Company's 5% Preferred Stock classified by the number of shares held:

Holders of		Number of Holders
1 to	10 shares	3,773
11 to	25 shares	1,151
26 to	50 shares	529
51 to	100 shares	336
101 to	500 shares	175
501 to	1,000 shares	11
Over	1,000 shares	10

Dividend Record and Profits in Relation to Preferred Stock:

The Company's 5% Preferred Stock came into existence May 29, 1935, replacing in part a 6½% issue of the same amount. All dividends on this 5% Preferred Stock since date of issue have been paid on the regular dividend dates. Consolidated net profits of the Company for each full year since

date of issue expressed in terms of ratio to preferred stock dividend requirements and of profit per share of preferred stock outstanding have been:

	Profit Times Preferred Stock Dividend Requirements	Profit Per Share of Preferred Stock
1941	4.5	\$22.30
1940	3.5	17.57
1939	3.0	15.01
1938	1.9	9.63
1937	2.5	12.50
1936	2.9	14.49

Company Net Worth in Relation to Preferred Stock:

The net worth of the Company — total assets minus total liabilities, reserves and unearned income — as reflected by balance sheets at the close of each full year since the Company's 5% Preferred Stock was originally issued, shows the Company's net worth, expressed in terms of dollars net worth per share of preferred stock outstanding, to have been:

1941	\$198.38
1940	184.36
1939	175.30
1938	163.71
1937	158.88
1936	149.06

Present Sinking Fund Obligation:

So long as the Company has outstanding any of its Fifteen-Year 4½% Debenture Bonds, due April 1, 1950, the annual sinking fund obligation of the 5% Preferred Stock is to purchase and cancel such stock at cost prices amounting in total to not less than 10% of consolidated net profit of the preceding year after deducting preferred stock dividends and sinking fund requirements on the 1950 debentures. The sinking fund requirement on the 1950 debentures in turn is 15% of consolidated net profit before deducting any dividends or sinking fund requirements.

The following tabulation shows the sinking fund obligation on the Company's 5% Preferred Stock for each of the last five years and the number of shares canceled and to be canceled by the use of this fund:

	Amount of Fund	Number of Shares Canceled
1941	\$362,852	4,771
1940	225,611	3,344
1939	177,037	2,700
1938	73,816	1,252
1937	130,841	1,644

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Future Sinking Fund Obligation:

Since all of the Fifteen-Year 4½% Debenture Bonds, due April 1, 1950, will have been retired and canceled by July 1, 1942, the sinking fund on the 5% Preferred Stock becomes 25% of consolidated net profit, after deducting preferred stock dividend requirements, from and after February 1, 1942. The effect of this change is best shown by example. The sinking fund requirement on the 5% Preferred Stock based upon consolidated net profit for the year ended January 31, 1942, was \$362,852. Had the current sinking fund requirement been applicable, this amount would have been \$1,033,202.

Conclusion:

In summary, the 5% Preferred Stock has (a) a consistent record of dividend payments since the date of issue, (b) a substantial margin of profits in excess of dividend requirements, (c) a constantly increasing net worth, and (d) an impending probable increase in sinking fund requirements of substantial proportions.

THE COMPANY'S COMMON STOCK

Holdings

There were no changes during the year in the total number of shares of common stock outstanding. According to the stock records of the Company and eliminating the stock in the names of brokers and known nominees held for an unknown number of people, the following summary shows the number of the holders of the Company's common stock classified by the number of shares held:

Holders of	Number of Holders
1 to 25 shares	5,922
26 to 50 shares	2,222
51 to 100 shares	2,609
101 to 500 shares	1,135
501 to 1,000 shares	127
1,001 to 5,000 shares	54
Over 5,000 shares	22

Net Asset Value

The net asset value at the close of the year applicable to the common stock of the Company — total tangible assets minus all liabilities, reserves, and the par value of preferred stock outstanding — as set forth in the consolidated balance sheet was \$23,353,597, or the equivalent of \$12.85 per share of such stock outstanding. Comparisons as of the close of each of the past five years follows:

	Total Net Asset Value	Net Asset Value Per Share Outstanding
1941	\$23,353,597	\$12.85
1940	19,192,410	10.56
1939	17,236,303	9.49
1938	14,781,300	8.17
1937	13,683,951	7.57

Use of 1941 Profit

Preferred stock dividends paid, \$1,161,450, deducted from consolidated net profit for the year, \$5,294,258, leaves a profit applicable to common stock of \$4,132,808. Of this amount the following approximate amounts were used: \$200,000 to repurchase preferred stock for cancellation in accordance with its sinking fund requirements; \$800,000 for principal payments on the funded debt and long-term obligations of the company and its subsidiaries; \$475,000 to pay for the cost of additions and improvements to property in excess of provision for depreciation; \$400,000 to pay the cash portion of the purchase price of the capital stock of B. Gertz, Inc.; and the balance of

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\$2,275,000 to finance in part the increased inventory and accounts receivable investment made necessary by increased sales volume and general merchandise market conditions.

Prospective Cash Requirements

Annual preferred stock dividend requirements are approximately one million two hundred thousand dollars. The average annual requirement for payments on funded debt and long-term obligations of the Company over the next few years will approximate one million dollars. The annual sinking fund obligation for the purchase of preferred stock in future years, assuming an annual profit equal to 1941, will approximate one million dollars. Total obligation for preferred stock dividends and retirement of senior securities will average close to three million dollars annually on the above basis. Increased need for working capital due to increases in sales volume in the past has usually been met by increased profit resulting from such sales. This may not be possible in the prospective semi-controlled economy of the future. Sales may increase more rapidly than profits due to many possible profit-restricting influences resulting from government actions or policies, the most apparent and important of which is tax and price-fixing legislation. The burden of such a condition will fall most heavily on companies, such as this one, with no excess working capital at present and with relatively large senior security issues outstanding. Interest charges and annual principal payments on funded debt and long-term obligations, together with dividend and sinking fund requirements on preferred stock issues, place definite limitations on the ability of the Company to increase working capital from profits.

Common Stock Dividends

The board of directors declared a dividend of fifteen cents per share on the common stock of the Company, payable April 20, 1942. Another dividend of like amount has been declared, payable July 20, 1942. While it is the hope of the board of directors that other similar actions may be taken at regular intervals, such actions must of necessity depend on the Company's sales volume and profit showing, its cash and working capital position and the general business conditions and outlook at the time. Existing circumstances make it impossible to forecast for the future regarding any one of these factors with any degree of certainty.

PROBLEMS OF THE RETAILER IN THIS WAR ECONOMY

The retailer today is faced with many new and strange problems. Only recently an oversupply of merchandise, an excess of manufacturing capacity, extreme unemployment and a shortage of consumer purchasing power were considered the problems of the greatest magnitude. This picture has changed to one of shortages of materials, manufacturing capacities, merchandise and manpower. Consumer purchasing power promises soon to surpass the supply of consumer goods, if it has not already done so. These shifts in the balance or lack of balance between the supply of consumer goods and consumer purchasing power create profound changes in the functioning of retailing. The major problems of the retailer today, in addition to doing everything possible to help win the war, are:

1. To assure a continuing supply of an adequate quantity of desirable merchandise for the public which the retailer represents as its purchasing agent;
2. To absorb the impact of changes in price levels and of efforts to control prices;
3. To maintain an adequate force of well-trained personnel; and
4. To meet tax payments and still maintain a financial position adequate to provide for the necessary investment in merchandise and accounts receivable and serve as a cushion for the inevitable period of readjustment.

Supply of Merchandise

The demand for consumer merchandise is always great in periods of full employment at relatively high wage rates. The present is such a period. The manufacture of war goods has absorbed much of the materials, machine capacity and labor that would otherwise have been available to meet increased demand for consumer goods. Shortages in certain lines of consumer goods—those lines most closely related to types of production required for the war effort—have developed.

Certain entire industries of consumer goods manufacturing have been converted to the manufacture of war goods. Merchandise formerly manufactured by such industries will no longer be available when existing supplies have been exhausted. Approximately 10% of this Company's sales volume has been in such merchandise.

Other industries formerly manufacturing consumer merchandise for civilian needs exclusively are devoting a certain part of their capacity to the manufacture of war needs. Shortages of materials and labor further curtail pro-

duction for civilian use. Much consumer merchandise must also be made available to our allies. Simplification and standardization of design and specification together with substitution of materials furnish part, but only a part, of the answer.

There are many reasons to expect a continuing progressive restriction of the supply of goods for civilian use. This restriction will inevitably affect adversely the sales volume of the retailer. Rationing will no doubt become necessary in connection with goods of a necessary character of which there is an inadequate supply. Rationing to the consumer will result in many complications for the retailer.

Price Trends

Consumer purchasing power far in excess of the supply of consumer goods creates an economic problem of the first magnitude for all and a particularly hazardous one for the mass consumer. Most retailers depend to a very substantial degree on the mass consumer. This problem therefore has special significance for the retailer. If this excess purchasing power is permitted to bid for the limited supply of consumer goods, inflationary increases in prices are bound to occur. Increased living costs for the mass consumer will result. The retailers' profits will be only paper profits, as they will of necessity have to be reinvested in inventory to finance the higher price levels of merchandise.

The retailer has recognized the harmful effects of higher prices and has endeavored to resist price advances at all points. As a part of this program, most retailers have followed a policy of pricing their merchandise on an original or an average cost basis rather than on a replacement cost basis. As a consequence, retail prices are approximately 9% lower than they would have been had such prices been based on a replacement cost basis. The President of the United States recently announced a seven-point program in relation to this price problem. The Office of Price Administration issued an order freezing prices at the manufactured, wholesale and retail levels each as of the same base period, the month of March, 1942.

The price freezing order as issued attempts to freeze prices without freezing the primary cost elements of materials and labor and disregards the important element of "time" as a factor in pricing. In many instances, material and labor costs are already much higher than were those costs that served as a base for establishing the price that has been frozen. Further increases in these cost elements are not only possible but highly probable. Disregarding the "time" element as a factor in pricing has resulted in gross inequities in all those instances in which the base period selling price was not based on replacement cost as of that period. Those who have avoided the replacement cost basis of pricing in an effort to keep prices down are heavily penalized as a result.

Personnel

Over the past several years wage levels in retailing have increased and working hours have been shortened. A study of hourly wage levels of office workers and salespeople in this Company discloses that the average hourly wage has increased 30% in the past five years. The current demand for workers by war industries and the unavoidable depletion of organizations by calls to military and other government services further complicate the personnel problems of the retailer.

Taxes

Taxes, federal, state and local, have taken an ever-increasing proportion of the income of this and all other companies over the past several years. In 1935 when consolidated net profit was \$1,581,759 total taxes paid were approximately one and three-quarter million dollars. In 1939 when consolidated net profit was \$3,435,585 total taxes amounted to approximately three million dollars. In 1941 with a consolidated net profit of \$5,294,258 total taxes paid amounted to almost seven and one-half million dollars.

To the extent that taxes paid are used to help win the war the Company gladly makes this contribution. It is mentioned here so that stockholders may appreciate the extent to which they are contributing indirectly to the cost of government and the war effort through their stock ownership. With government expenditures and borrowings running at unprecedented figures there is every indication that the tax burden of the future will continue to take a very heavy toll from all corporations.

ALLIED STORES CORPORATION AND SUBSIDIARIES

Consolidated Balance Sheet — January 31, 1942

ASSETS

Current Assets:

Cash	\$3,636,067.64	
Accounts and notes receivable:		
Customers:		
Current accounts	\$14,463,327.91	
Deferred payment accounts and notes		
(Note A)	8,769,886.94	
	<u>\$23,233,214.85</u>	
Equity in deferred payment accounts		
(\$1,600,751.59) sold	240,112.82	
Total	\$23,473,327.67	
Less reserve	1,023,866.81	22,449,460.86
Accounts receivable — suppliers and sundry debtors	580,186.61	
Merchandise inventories, including \$2,928,842.31 for merchandise in transit, at mills, etc. (Note B)	24,215,447.94	
Total current assets		\$50,881,163.05

Other Assets:

Insurance and other deposits	\$ 219,526.86	
Investments and real estate	207,046.38	
Sundry notes and accounts receivable	657,524.60	
Common stock of Allied Stores Corporation—12,271 shares at cost—market value \$69,024 (Note C)	141,419.82	
Total other assets		1,225,517.66

Land, Buildings, Equipment, Etc. (Notes D and E):

Land	\$18,638,536.51	
Buildings and equipment	\$12,678,679.30	
Less reserve for depreciation	3,820,451.19	8,858,228.11
Store fixtures and equipment	\$10,445,749.61	
Less reserve for depreciation	5,505,864.81	4,939,884.80
Improvements to leased property	\$ 1,840,513.57	
Less reserve for depreciation	415,386.27	1,425,127.30
Total land, buildings, equipment, etc.		33,861,776.72

Deferred Charges:

Unexpired insurance premiums	\$ 287,672.62	
Prepaid rent and taxes	292,561.36	
Inventory of supplies	805,040.19	
Prepaid service contracts, improvements in process, travel advances, etc.	266,552.19	
Unamortized portion of bond discount and expenses	162,279.77	
Total deferred charges		1,814,106.13

Goodwill and Other Intangible Assets 1.00

\$87,782,564.56

ALLIED STORES CORPORATION AND SUBSIDIARIES

Consolidated Balance Sheet — January 31, 1942

LIABILITIES

Current Liabilities:

Notes payable to banks—for current loans	\$ 2,900,000.00	
Accounts payable for merchandise, etc. (Note B)	8,355,346.84	
Accrued accounts	2,497,407.51	
Taxes (other than federal taxes on income)	1,460,723.31	
Federal taxes on income—estimated (Note B)	4,298,998.43	
Installments on mortgages and long term notes, and sinking fund payments due within one year	803,273.76	

Total current liabilities		\$20,315,749.85
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Funded Debt and Long Term Obligations:

Per schedule, with notes, attached:		
Allied Stores Corporation	\$ 6,363,375.00	
Less included in current liabilities	507,375.00	\$ 5,856,000.00
Subsidiaries	\$13,096,469.19	
Less included in current liabilities	294,478.76	12,801,990.43

Total funded debt		18,657,990.43
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Reserves:

For contingencies	\$ 500,000.00	
Miscellaneous	657,486.95	

Total reserves		1,157,486.95
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Deferred Credits:

Discount on bonds of subsidiary company held by Allied Stores Corporation	\$ 57,574.03	
Unearned carrying charges on deferred payment accounts	501,865.84	

Total deferred credits		559,439.87
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Capital Stock and Surplus:

Capital Stock:		
Preferred Stock — cumulative — par value		
\$100 per share:		
Authorized — 600,000 shares		
Issued — 5% Preferred Stock — re- deemable at and entitled upon liquid- ation to \$100 per share (Notes F and G)	\$23,918,600.00	
Less in treasury	180,300.00	\$23,738,300.00

Common Stock — without par value:		
Authorized — 2,500,000 shares (Note G)		
Issued — 1,817,153 shares — capital fixed by Board of Directors at \$1.00 per share		1,817,153.00

Surplus (Note H):		
Capital	\$10,259,590.68	
Earned (from June 1, 1935 to January 31, 1942) (Note B)	11,276,853.78	21,536,444.46

Total capital stock and surplus		47,091,897.46
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Contingent liabilities, etc. (Note I)		
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		\$87,782,564.56
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Notes to financial statements follow hereafter.

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ALLIED STORES CORPORATION AND SUBSIDIARIES

Consolidated Statement of Profit and Loss for the Fiscal Year Ended January 31, 1942

Net sales (including leased departments)		\$151,808,858.36	
Cost of goods sold (Note B)		99,302,918.92	
Gross margin			\$ 52,505,939.44
Operating expenses:			
Administrative, buying, rent and other occupancy costs, publicity, selling and general expenses, including provision for doubtful accounts (less income of \$705,859.34 from carrying charges on deferred payment accounts)	\$39,846,925.98		
Provision for depreciation	1,364,813.96		
Maintenance and repairs	1,107,499.60	42,319,239.54	
Operating profit			\$ 10,186,699.90
Other income:			
Recovery of tax and other claims applicable to prior years	\$ 119,542.94		
Miscellaneous	272,007.99	391,550.93	
			\$ 10,578,250.83
Other deductions:			
Expenses incident to liquidation of subsidiary company	\$ 78,124.74		
Miscellaneous	67,874.80	145,999.54	
			\$ 10,432,251.29
Interest:			
Subsidiaries:			
On mortgage bonds, long term notes and mortgages (including \$6,876.94 for amortization of bond discount and expense)	\$582,134.85		
Other	17,600.08	\$ 599,734.93	
Allied Stores Corporation:			
On debenture bonds, long term notes and mortgage (including \$10,076.04 for amortization of bond discount and expense)	\$254,163.64		
Other	84,094.87	338,258.51	937,993.44
Profit before federal taxes on income			\$ 9,494,257.85
Provision for estimated federal taxes on income (Note B):			
Normal income tax and surtax	\$ 2,133,000.00		
Excess profits tax	2,067,000.00	4,200,000.00	
Consolidated net profit (Note B)			\$ 5,294,257.85

Notes to financial statements follow hereafter.

ALLIED STORES CORPORATION AND SUBSIDIARIES

Consolidated Statement of Earned and Capital Surplus for the Fiscal Year Ended January 31, 1942

	<u>Earned</u>	<u>Capital</u>
Balance—January 31, 1941	\$ 8,341,670.23	\$ 9,033,586.82
<i>Add:</i>		
Consolidated net profit	5,294,257.85	
Discount on repurchase of 5% Preferred Stock		54,216.97
Transfer from reserve for contingencies		1,171,786.89
	<u>\$13,635,928.13</u>	<u>\$10,259,590.68</u>
<i>Deduct:</i>		
Dividends paid in cash on 5% Preferred Stock—at rate of \$5.00 per share per annum	1,161,450.42	
Elimination of cash discounts from amounts of inventories and merchandise accounts payable at January 31, 1941 (Note B)	697,623.93	
Excess of cost of capital stock of subsidiary over equity in its tangible net assets at date of acquisition	500,000.00	
	<u>\$ 2,359,074.35</u>	
Balance—January 31, 1942 (Note H)	<u>\$11,276,853.78</u>	<u>\$10,259,590.68</u>

Consolidated Statement of Reserve for Contingencies for the Fiscal Year Ended January 31, 1942

Balance—January 31, 1941	\$ 1,671,786.89
Transferred to capital surplus	1,171,786.89
Balance—January 31, 1942	<u>\$ 500,000.00</u>

Notes to financial statements follow hereafter.

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NOTES TO FINANCIAL STATEMENTS

Note A: Customers' conditional sales notes and deferred payment accounts include carrying charges. Installments maturing later than one year from the date of the balance sheet have been included in current assets in accordance with trade practice.

Note B: Amounts for inventories of merchandise have been stated (1) with respect to merchandise on hand, at the lower of cost or market by the retail inventory method (except for a comparatively small amount of inventories taken generally at invoice cost), and using the "last-in, first-out" principle based upon published indexes of price changes since January 31, 1941, in determination of cost of certain merchandise inventories, and (2) with respect to merchandise in transit, at mills, etc., at invoice cost or average cost. The inventory amounts generally are also net of discounts.

The method of determining amounts of merchandise inventories was changed during the year by eliminating cash discounts and by the adoption of the "last-in, first-out" principle with respect to pricing certain merchandise inventories.

The effect of such change at January 31, 1942, has been:

- (1) To reduce the amounts for merchandise inventories by \$2,351,955.07, representing elimination of cash discounts — \$1,075,616.07; and application of "last-in, first-out" principle of cost determination — \$1,276,339.00;
- (2) To reduce merchandise accounts payable by \$187,511.14 for applicable cash discounts;
- (3) To reduce consolidated net profit before taxes on income, by \$1,466,820.00, representing change in treatment of cash discounts—\$190,481.00; and application of "last-in, first-out" principle of cost determination—\$1,276,339.00;
- (4) To reduce provision for federal taxes on income by \$775,000.00;
- (5) To reduce consolidated net profit after taxes by \$691,820.00;
- (6) To charge earned surplus \$697,623.93 (net) for cash discounts applicable to the inventories and merchandise accounts payable at January 31, 1941.

The provision for federal taxes on income has been made on the basis of applying the "last-in, first-out" principle of determining the amounts of certain merchandise inventories, instead of the method heretofore used, but without giving effect to the change in accounting for cash discounts. In the event use of such principle is not permitted for tax purposes for the fiscal year ended January 31, 1942, then the taxable income of the constituent companies will be increased by \$1,276,339, and the liability for federal taxes on income will be increased by \$775,000.

Note C: These shares are held by Allied Purchasing Corporation (a subsidiary) for resale to certain employees. Options to purchase these shares were granted to twenty-seven employees and two officers, no individual holding options for more than 950 shares. The option price of said shares is \$11.00 per share and the options may be exercised and the shares paid for from time to time in whole or in part on or before June 30, 1942, and, if not exercised by that date, the options shall lapse.

Note D: The carrying amounts for land, buildings, store fixtures, equipment, etc., are as follows:

1. Properties held by certain subsidiaries at dates of acquisition, at amounts shown by their books which, so far as is known, represented cost to the subsidiaries, except for a reduction in 1940 of \$981,957.52 in the carrying amount of real estate of one subsidiary to amount paid (based on independent appraisals) by another subsidiary on inter-company sale; or
2. At cost to the consolidated group measured by the cash cost to the Corporation of securities of a certain real estate subsidiary; or
3. At amounts shown by the books of certain subsidiaries at the dates of acquisition of their capital stocks by the Corporation, less part of the amount by which the cost of capital stocks was less than the equity in such subsidiaries' net assets, as shown by their books at the time they were acquired by the Corporation, (the balance of such amount of excess equity is included in capital surplus); and
4. Subsequent additions to the properties at cost.

Note E: Land, buildings and equipment, and store fixtures carried in the consolidated balance sheet at \$30,214,707, less related reserves for depreciation of \$3,783,414, are subject to mortgages and mortgage bond obligations totaling \$12,728,037.

Note F: On or before July 1st, each year, the Corporation under its charter is obligated to apply as a sinking fund to the purchase or redemption of its 5% Preferred Stock a sum equal to 10% of consolidated net earnings for the previous fiscal year after deducting dividends on its 5% Preferred Stock and sinking fund requirements upon its Fifteen-Year 4½% Debenture Bonds, due April 1, 1950; and, after all such debenture bonds have been retired, a sum equal to 25% of consolidated net earnings for the previous fiscal year after deducting such dividends. The sinking fund payment due on July 1, 1942, amounts to \$362,852 against which the Corporation may apply (1) 1,803 shares of 5% Preferred Stock, held in treasury, acquired at a cost of \$144,015 and (2) such part of 3,000 shares of 5% Preferred Stock purchased after January 31, 1942, at a cost of \$221,036, as is required to meet such sinking fund obligation.

Note G: At the option of any of the holders of \$548,432 principal amount of 5½% Income Bonds of C. C. Anderson Stores Company (a subsidiary), Allied Stores Corporation agrees to acquire such income bonds at any time prior to August 1, 1942, at the principal amount thereof (with cash adjustment of accrued interest), and issue in exchange therefor its own 5% Preferred Stock or Common Stock, as such holders may elect, on the basis of \$100 per share for the 5% Preferred Stock of Allied Stores Corporation (with cash adjustment of accrued dividends), and \$30 per share for the Common Stock of Allied Stores Corporation.

Note H: Upon the basis of treating \$180,300 par value 5% Preferred Stock in the treasury as though retired.

Note I: Contingent liabilities, etc.:
Subsidiary companies:

1. The terms of a ground lease as modified by an agreement dated October 1, 1940 require that on or before October 1, 1945 (or at a later date under certain circumstances), the lessee shall, at its option, either (a) erect a new building or (b) rehabilitate the buildings situated on such leased premises on October 1, 1940, at a cost, in either case, of not less than \$400,000; said obligation is guaranteed by Allied Stores Corporation.
2. Under the terms of another ground lease as modified by an agreement dated April 14, 1936, in the event of default in any of the provisions of the modifying agreement prior to November 1, 1947 (the modified terminal date of the lease), the provisions of the original lease shall immediately become effective, and the company shall be liable:
 - (a) For the full annual cash rent of \$24,000 (reduced to \$16,500 annually by the modifying agreement) for the period from November 1, 1936, to the expiration of the original lease, November 1, 2021, and
 - (b) For the erection of a building at a cost of not less than \$200,000 (from the erection of which it is otherwise relieved by the modifying agreement).
3. As endorsers on customers' notes for loans from banks and finance companies aggregating approximately \$13,635.00, and as guarantor of installment contracts sold to finance companies aggregating \$17,825.12.
4. Unused balance of \$75,069.76 of letters of credit.

ALLIED STORES CORPORATION AND SUBSIDIARIES *Funded Debt and Long Term Obligations—January 31, 1942*

Obligor	Description	Amount Authorized by Indenture	Amount Unissued	Amount Retired Through Sinking Fund or Cancelled	Amount in Treasury of Corporation and Subsidiaries Consolidated	Amount Outstanding as per Consolidated Balance Sheet	Amount due Within One Year
Allied Stores Corporation:	Debtenture Bonds						
	Fifteen-Year 4½% Debenture Bonds, due April 1, 1950 —	\$ 3,337,000	\$ 182,020	\$2,983,340	\$ 96,265	\$ 75,375.00	Note A
	4½% Debentures due 1951 —	10,000,000	4,800,000	820,000	32,000	4,348,000.00	Note B
	Long Term Notes						
	Due 1942 to 1946 (1½% to 2%)					1,250,000.00	250,000.00
	Real Estate Mortgage						
	Due 1947—(4% to 4½%) Note C					690,000.00	40,000.00
Subsidiaries:	Bonds						
	C. C. Anderson Stores Company 5½% Income Bonds, due April 1, 1972	750,000	{ 160,622	19,553	21,393	548,432.00	Note D
	Geo. B. Peck, Inc. Seven Year Income 5% Debentures (Sinking Fund), due April 1, 1946	300,000	None	None	290,000	10,000.00	Note E
	Mortgage Bonds						
	Jordan Marsh Company First Mortgage and First Lien 3¾% Sinking Fund Bonds, due August 15, 1956	6,000,000	None	1,077,000	None	4,943,000.00	Note F
	Real Estate Mortgages						
	Allied Real Estate Trust Due 1959—(4% to 4½%)					1,500,000.00	None
	Allied Real Estate Trust Due 1954—(4%)					500,000.00	None
	C. C. Anderson Stores Company Due 1962—(4½%)					269,287.09	8,062.09
	Jordan Marsh Company Due 1949—(4%)					138,750.00	4,500.00
	Joske Bros. Co. Due 1959—(4% to 4½%)					1,100,000.00	None
	C. F. Hovey Company Due 1951—(3%)					44,500.00	5,000.00
	The Polsky Realty Company Due 1945—(4½%)					892,500.00	22,500.00
	Pomeroy's, Inc. Due 1959—(4%)					1,650,000.00	None
	Pomeroy's, Inc. Due 1949—(4½% to 4%)					350,000.00	None
	The Tiche-Goettinger Company Due 1944—(5½%)					650,000.00	50,000.00
	Long Term Notes						
	Allied Real Estate Trust Due 1944—(2½%)					250,000.10	83,333.34
	The Polsky Realty Company Due 1945—(2%)					250,000.00	27,083.33
						<u>\$19,459,844.19</u>	<u>\$801,853.76</u>

Notes to funded debt follow hereafter

NOTES TO FUNDED DEBT

Allied Stores Corporation:

Note A: The Indenture relating to Fifteen-Year 4½% Debenture Bonds, due April 1, 1950, provides for a sinking fund payable on April 15th of each year equivalent to 15% of consolidated net earnings for the preceding fiscal year. Sinking fund payment required on April 15, 1942, was fulfilled by applying, (1) balance of \$334,944.10 representing cost of bonds retired on April 15, 1941, in excess of sinking fund requirement on that date, (2) \$96,265 principal amount of bonds purchased by the Corporation for \$93,971.25 and held by the trustee, and (3) deposit with trustee on April 15, 1942, of \$76,222.97 for the redemption of the remaining \$75,375 principal amount of outstanding bonds with accrued interest to July 1, 1942.

Note B: The Indenture relating to 4½% Debentures due 1951 provides for a sinking fund payable on May 20th each year equal to the sinking fund redemption price of 3⅓% of the greatest aggregate principal amount of said bonds which shall ever have been authenticated by the trustee. Sinking fund payment due on May 20, 1942, amounts to \$175,067 against which there may be applied \$32,000 principal amount of bonds (at 101%) purchased by the Corporation and held by the trustee pending cancellation to fulfill such sinking fund requirement.

Note C: Mortgage of Dey Brothers & Co. assumed by Allied Stores Corporation upon merger of that subsidiary.

Subsidiary Companies:

Note D: The Indenture relating to 5½% Income Bonds due 1972 of C. C. Anderson Stores Company provides for redemption of the bonds at any time, in whole or in part, at the option of said Company at the principal amount thereof. Interest on the bonds is cumulative, but is required to be paid currently only if, and to the extent that, there are available net earnings of its last previously completed semi-annual fiscal period. The said Company agrees that so long as any of these bonds shall remain outstanding it will not issue any additional 5½% Income Bonds without consent of the registered holders of a majority in principal amount of the bonds at the time outstanding. Reference is made to Note G to financial statements.

Note E: Subsequent to January 31, 1942 Allied Stores Corporation purchased the remaining \$10,000 principal amount of these bonds outstanding at that date; accordingly no provision has been made for sinking fund payment required on March 1, 1942.

Note F: The Supplemental Indenture dated August 15, 1941, relating to First Mortgage and First Lien 3¾% Sinking Fund Bonds due August 15, 1956, of Jordan Marsh Company provides for a payment for interest and sinking fund of \$110,681 on February 15, 1942, and \$168,750 semi-annually thereafter beginning August 15, 1942. These bonds are guaranteed as to principal and interest by Andrews Real Estate Trust, a subsidiary of the Corporation, which owns a substantial part of the premises occupied by Jordan Marsh Company.

Note G: The real estate mortgage of C. C. Anderson Stores Company provides for the payment of a sum equal to certain percentages of net sales made on the mortgaged premises for each twelve month period commencing September 1st, but in no event less than \$24,000 for each such period, such minimum to be payable in monthly installments. The amount paid for each twelve month period in excess of interest at the rate of 4½% per annum on said mortgage is applied against the principal.

ERNST & ERNST

NEW YORK

19 RECTOR STREET

May 7, 1942.

BOARD OF DIRECTORS,
ALLIED STORES CORPORATION,
New York, New York.

We have examined the consolidated balance sheet of ALLIED STORES CORPORATION and subsidiaries as of January 31, 1942, and the consolidated statements of profit and loss for the fiscal year then ended, have reviewed the systems of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence, by methods and to the extent we deemed appropriate. Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances and included all procedures which we considered necessary.

In our opinion, the accompanying consolidated balance sheet and related consolidated statements of profit and loss and surplus present fairly the position of ALLIED STORES CORPORATION and its subsidiaries at January 31, 1942, and the consolidated results of their operations for the year, in conformity with generally accepted accounting principles which, except for the change (which we approve) in the method of pricing inventories and stating merchandise accounts payable as set forth in Note B to financial statements, were applied on a basis consistent with that of the preceding year.

ERNST & ERNST.

thirty-seven

ALLIED STORES CORPORATION AND SUBSIDIARIES

Comparative Consolidated Balance Sheets—January 31, 1938-1942

ASSETS	January 31				
	1938	1939	1940	1941	1942
Current Assets:					
Cash	\$ 2,597,419	\$ 4,034,161	\$ 2,164,136	\$ 2,616,077	\$ 3,636,068
Accounts and notes receivable (net)	17,374,482	16,335,227	17,874,340	18,687,335	23,029,647
Merchandise inventories	15,433,392	14,758,424	17,390,733	18,399,979	24,215,448
Total current assets	35,405,293	35,127,812	37,429,209	39,703,391	50,881,163
Land, Buildings, Equipment, Etc.:					
Land	16,880,400	16,982,901	19,579,536	18,624,178	18,638,537
Buildings and equipment (net)	7,243,246	8,235,999	9,153,537	8,883,484	8,858,228
Store fixtures and equipment (net)	3,714,019	3,416,251	4,057,585	4,350,863	4,939,885
Improvements to leased property (net)	539,000	621,070	1,264,100	1,401,235	1,425,127
Total land, buildings, equipment, etc.	28,376,665	29,256,221	34,054,758	33,259,760	33,861,777
Other Assets	748,797	749,449	771,918	907,098	1,225,518
Deferred and Prepaid Expenses	821,726	862,568	975,258	1,009,741	1,651,826
Unamortized Portion of Bond Discount and Expense	232,239	203,635	180,605	157,358	162,280
Good Will and Other Intangible Assets	1	1	1	1	1
Total assets	<u>\$65,584,721</u>	<u>\$66,199,686</u>	<u>\$73,411,749</u>	<u>\$75,037,349</u>	<u>\$87,782,565</u>

LIABILITIES

Current Liabilities:					
Notes payable to banks — for current loans	\$ —	\$ —	\$ 800,000	\$ 900,000	\$ 2,900,000
Other current liabilities	7,126,163	7,281,890	9,311,510	10,107,864	17,415,750
Total current liabilities	7,126,163	7,281,890	10,111,510	11,007,864	20,315,750
Funded Debt and Long Term Obligations (exclusive of amounts included under current liabilities)	19,281,852	18,509,818	20,732,712	19,439,913	18,657,990
Reserves	1,784,285	2,030,544	2,052,229	2,179,112	1,157,487
Unearned Income	468,370	396,034	388,895	467,950	559,440
Capital Stock and Surplus:					
5% Preferred Stock—par value \$100 per share—outstanding	23,240,100	23,200,100	22,890,100	22,750,100	23,738,300
Common stock and surplus	13,683,951	14,781,300	17,236,303	19,192,410	23,353,598
Total capital stock and surplus	36,924,051	37,981,400	40,126,403	41,942,510	47,091,898
Total liabilities	<u>\$65,584,721</u>	<u>\$66,199,686</u>	<u>\$73,411,749</u>	<u>\$75,037,349</u>	<u>\$87,782,565</u>

thirty-eight

ALLIED STORES CORPORATION AND SUBSIDIARIES

Comparative Consolidated Statements of Profit and Loss, Earned Surplus, and Capital Surplus for the Fiscal Years Ended January 31, 1938-1942

Profit and Loss for the Fiscal Year Ended January 31

	1938	1939	1940	1941	1942
Net sales (including leased departments)	\$107,556,225	\$103,243,425	\$112,122,354	\$121,270,682	\$151,808,858
Gross margin	36,965,915	34,985,055	38,370,942	41,417,929	52,505,940
Operating expenses:					
Provision for depreciation	1,182,692	1,189,427	1,264,588	1,290,135	1,364,814
Maintenance and repairs	624,289	557,055	743,135	728,798	1,107,500
All other operating expenses	30,726,088	29,651,588	31,491,864	33,453,540	39,846,926
Total operating expenses	32,533,069	31,398,070	33,499,587	35,472,473	42,319,240
Operating profit	4,432,846	3,586,985	4,871,355	5,945,456	10,186,700
Other income (net)	226,276	60,481	248,388	366,343	245,551
	4,659,122	3,647,466	5,119,743	6,311,799	10,432,251
Interest charges	985,916	888,745	964,158	958,670	937,993
Profit before federal taxes on income	3,673,206	2,758,721	4,155,585	5,353,129	9,494,258
Provision for estimated federal taxes on income	769,000	525,000	720,000	1,355,000	4,200,000
Consolidated net profit	\$ 2,904,206	\$ 2,233,721	\$ 3,435,585	\$ 3,998,129	\$ 5,294,258

EARNED SURPLUS

Balance at beginning of period	\$ 1,364,832	\$ 3,108,875	\$ 4,182,091	\$ 6,467,796	\$ 8,341,670
Add—					
Consolidated net profit	2,904,206	2,233,721	3,435,585	3,998,129	5,294,258
Total	4,269,038	5,342,596	7,617,676	10,465,925	13,635,928
Deduct—					
Dividends paid on 5% Preferred Stock	1,160,163	1,160,505	1,149,880	1,142,297	1,161,450
Reducing carrying amount of real estate on intercompany sale	—	—	—	981,958	—
Elimination of cash discounts from inventories and accounts payable	—	—	—	—	697,624
Excess of cost of subsidiary over equity in its net assets at date of acquisition	—	—	—	—	500,000
Total deductions	1,160,163	1,160,505	1,149,880	2,124,255	2,359,074
Balance at end of period	\$ 3,108,875	\$ 4,182,091	\$ 6,467,796	\$ 8,341,670	\$ 11,276,854

CAPITAL SURPLUS

Balance at beginning of period	\$ 8,390,854	\$ 8,766,923	\$ 8,791,056	\$ 8,951,354	\$ 9,033,587
Add—					
Discount on repurchase of 5% Preferred Stock	62,030	24,133	106,329	82,233	54,217
Excess of equity in net assets of subsidiaries at dates of acquisition	314,039	—	53,969	—	—
Transfer from reserve for contingencies	—	—	—	—	1,171,787
Balance at end of period	\$ 8,766,923	\$ 8,791,056	\$ 8,951,354	\$ 9,033,587	\$ 10,259,591

STORES OWNED BY ALLIED STORES CORPORATION

THE A. POLSKY COMPANY	Akron, Ohio
O'NEILL & COMPANY, INCORPORATED	Baltimore, Md.
JORDAN MARSH COMPANY	Boston, Mass.
C. F. HOVEY COMPANY	Boston, Mass.
THE ROLLMAN & SONS COMPANY	Cincinnati, Ohio
THE MOREHOUSE-MARTENS COMPANY	Columbus, Ohio
THE TITCHE-GOETTINGER COMPANY	Dallas, Texas
HERPOLSHEIMER COMPANY	Grand Rapids, Mich.
THE MEYER'S COMPANY	Greensboro, N. C.
THE L. H. FIELD COMPANY	Jackson, Mich.
B. GERTZ, INC.	Jamaica, N. Y.
GEO. B. PECK, INC.	Kansas City, Mo.
THE MULLER COMPANY, LIMITED	Lake Charles, La.
LOUIS SAMLER, INC. (THE BON TON)	Lebanon, Pa.
C. M. GUGGENHEIMER CORPORATION	Lynchburg, Va.
F. N. JOSLIN COMPANY	Malden, Mass.
L. S. DONALDSON COMPANY	Minneapolis, Minn.
QUACKENBUSH COMPANY	Paterson, N. J.
WAITE'S, INC.	Pontiac, Mich.
JOSKE BROS. CO.	San Antonio, Texas
THE BON MARCHÉ	Seattle, Wash.
HEER'S, INCORPORATED	Springfield, Mo.
THE GOLDEN RULE	St. Paul, Minn.
DEY BROTHERS & CO.	Syracuse, N. Y.
MAAS BROTHERS, INC.	Tampa, Florida
THE JAMES BLACK DRY GOODS COMPANY	Waterloo, Iowa
POMEROY'S, INC.	Reading, Pa.
(Operates stores in Reading, Harrisburg, Wilkes-Barre and Pottsville, Pa.)	
A. E. TROUTMAN COMPANY	Greensburg, Pa.
(Operates stores in Greensburg, Butler, Dubois, Indiana, Connellsville and Latrobe, Pennsylvania)	
C. C. ANDERSON STORES COMPANY	Boise, Idaho
(Branches in fifteen cities in Idaho, two cities in Oregon, two cities in Colorado, two cities in Utah and one city in South Dakota)	

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